Common Law Concepts of Life Insurance in Community Property Jurisdictions: Recommendations for a Practical Approach

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It should come as no surprise to legal practitioners that the 20th century has been a time of conflict and confusion regarding community property rights in life insurance policies.[1] Community property law, having originated in Europe,[2] is now the law in eight states: Arizona, California, Louisiana, New Mexico, Texas, Idaho, Nevada, and Washington.[3] The major principle underlying community property systems places ownership of any property acquired after marriage in the marital community, each spouse possessing an undivided one-half interest therein.[4] On the other hand, all property owned by a spouse before

1. *See* W. DE FUNIAK & M. VAUGHN, PRINCIPLES OF COMMUNITY PROPERTY § 79, at 189-90 (2d ed. 1971); S. SCOVILLE, COMMUNITY PROPERTY RIGHTS IN LIFE INSURANCE 4-6 (1969). *See generally* Lyons, *Development of Community Property Law in Arizona*, 15 LA. L. REV. 512 (1955).

2. Community property law is believed to have originated with the Germanic Goths when they began granting property rights to their women warriors as rewards for their feats in battle. W. DE FUNIAK & M. VAUGHN, *supra* note 1, §§ 7-13; S. SCOVILLE, *supra* note 1, at 4; Kirkwood, *Historical Background and Objectives of the Law of Community Property in the Pacific Coast States*, 11 WASH. L. REV. 1, 1 (1936). The Spanish and French, in turn, inherited community property concepts from the Goths during German occupation of their countries. *See, e.g.*, W. DE FUNIAK & M. VAUGHN, *supra* note 1, at § 8; S. SCOVILLE, *supra* at 4-6; Kirkwood, *supra*; Loewy, *The Spanish Community of Acquests and Gains and its Adoption and Modification by the State of California*, 1 CALIF. L. REV. 32, 32-34 (1912). *See generally* M. RUIZ, MEXICAN AMERICAN LEGAL HERITAGE IN THE SOUTHWEST 31-34 (1972).

3. *See* W. BROCKELBANK, THE COMMUNITY PROPERTY LAW OF IDAHO 14-18 (1962); W. DE FUNIAK & M. VAUGHN, *supra* note 1, § 37 at 55; S. SCOVILLE, *supra* note 1, at 1 & n.1; C. SMITH, 1974 SUMMARY OF ARIZONA COMMUNITY PROPERTY LAW § 2, at 3 (1974).

4. *See, e.g.*, King v. Uhlmann, 103 Ariz. 136, 151, 437 P.2d 928, 943 (1968); La Tourette v. La Tourette, 15 Ariz. 200, 205-06, 208, 137 P. 426, 428, 429 (1914); Rodieck v. Rodieck, 9 Ariz. App. 213, 222, 450 P.2d 725, 734 (1969); ARIZ. REV. STAT. ANN. §§ 25-211, -214 (Supp. Pamphlet 1973); CAL. CIV. CODE § 5105 (West Supp. 1976); IDAHO CODE § 32-906 (1963); NEV. REV. STAT. §§ 123.220, .225 (1975); N.M. STAT. ANN. §§ 57-4A-2(b), -8 (Supp. 1975); WASH. REV. CODE ANN. § 26.16.030 (Supp. 1976); *cf.* LA. CIV. CODE ANN. arts. 2334, 2402 (West 1971).

In Arizona property is deemed community or separate depending upon whether community or separate funds were used to purchase it. *See* Nace v. Nace, 104 Ariz. 20, 23, 448 P.2d 76, 79 (1968); Malich v. Malich, 23 Ariz. 423, 428, 204 P. 1020, 1022 (1922); Davis v. Davis, 9 Ariz. App. 49, 52, 449 P.2d 66, 69 (1969); ARIZ. REV. STAT. ANN. §§ 25-211, -213 (Supp. Pamphlet 1973). If the property is acquired after mar-

marriage or purchased after marriage with previously owned funds is designated separate and remains his or her sole property throughout the existence of the marital community.[5]

Unfortunately for the community property jurisdictions, the concept of life insurance and its concomitant laws developed under common law theories.[6] Until the 20th century, life insurance policies had no cash surrender value[7] if forfeited before death and seldom included the right to change the beneficiary, beneficiary designations being treated as irrevocable.[8] Policies were considered to be purely contractual between the insured and insurer with no property characteristics. Thus, if the insured failed to pay premiums for the period specified in the contract, the contract was terminated due to failure of consideration, leaving the insured with no interest in the policy or past premiums paid in.[9] As a form of contract, life insurance policies created no real problems for community property states, they were considered neither separate nor community property, merely an agreement to pay money at death.[10] The beneficiary was considered owner of the policy since the designation of a beneficiary could not be changed;

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riage and is moveable, the law of the jurisdiction where the spouses are domiciled at the time of the acquisition governs. *See* Jizmejian v. Jizmejian, 16 Ariz. App. 270, 272, 492 P.2d 1208, 1210 (1972); Rau v. Rau, 6 Ariz. App. 362, 364, 432 P.2d 910, 912 (1967). A subsequent move to a noncommunity property state will not alter this characterization. *See id.* at 364, 432 P.2d at 912. Nor will a transformation of the property from personalty to realty change its character. *See* Stephen v. Stephen, 36 Ariz. 235, 238, 284 P. 158, 159 (1930). Generally, once the character of property is determined it retains the same character unless changed by agreement of the spouses. *See* Armer v. Armer, 105 Ariz. 284, 287, 463 P.2d 818, 821 (1970); Porter v. Porter, 67 Ariz. 273, 281, 195 P.2d 132, 137 (1948). However, should the property become so commingled with property of another character that it is no longer identifiable, its character may change according to the nature of the property with which it is commingled. *See* Nace v. Nace, *supra* at 23, 448 P.2d at 79; Evans v. Evans, 79 Ariz. 284, 286-87, 288 P.2d 775, 777 (1955).

5. *E.g.*, Porter v. Porter, 67 Ariz. 273, 280, 195 P.2d 132, 136 (1948); *In re* Stark, 52 Ariz. 416, 420, 82 P.2d 894, 895-96 (1938); Woffenden v. Charauleau, 2 Ariz. 91, 92, 11 P. 117, 118 (1886); Roberts v. Roberts, 35 N.M. 593, 594-95, 4 P.2d 920, 920 (1931). *But see* Arnold v. Leonard, 114 Tex. 535, 539-42, 273 S.W. 799, 801-03 (1925).

6. S. SCOVILLE, *supra* note 1, at 5; Ray, *Life Insurance, Community Property and Death Taxes in Texas*, 26 TEX. B.J. 835, 835-36, 894 (1963).

7. Cash surrender value refers to a contractual right to some form of refund for premiums paid into an insurance policy should the insured decide to discontinue the policy.

> The cash surrender value of a life insurance contract has been defined as the cash value (as determined by rules set forth in the governing statute and the nonforfeiture section of the policy) of a policy that has been surrendered to the insurer by a person having the contractual right to surrender it.

J. GRIEDER & W. BEADLES, LAW AND THE LIFE INSURANCE CONTRACT 439 (3d ed. 1974). *See also* 3A J. APPLEMAN & J. APPLEMAN, INSURANCE LAW AND PRACTICE §§ 1751 & n.1, 1764 (1967).

8. *See* S. SCOVILLE, *supra* note 1, at 4-6; W. VANCE, LAW OF INSURANCE §§ 99, 106 (3d ed. 1951); Comment, *Insurance and the Community*, 25 LA. L. REV. 492, 492 n.11 (1965).

9. S. SCOVILLE, *supra* note 1, at 5.

10. *Id.* at 4-6; Comment, *supra* note 8, at 492. *See generally* S. KIMBALL, INSURANCE AND PUBLIC POLICY 3-5 (1960).

thus he had an interest in the proceeds superior even to that of the insured, whose only interest in the policy was the payment of premiums to assure that the beneficiary would recover the proceeds.[11]

During the last century, however, insurance policies began to carry cash surrender values, were made nonforfeitable, and allowed the insured to change the named beneficiary.[12] With this change in characteristics, life insurance policies and their proceeds came to resemble a form of property and are now universally treated as such by the courts.[13] Life insurance policies still retain their contractual nature between the insured and insurer: the premiums are consideration which support the insured's promise to pay at death or forfeiture. However, as to the insured, his or her spouse, and the beneficiary, the policy and its proceeds are treated as property in which any or all may have an interest. This judicial transition was problematical in the eight community property states because community property systems were not designed to accommodate common law life insurance concepts.[14] Additionally, since the treatment of life insurance as property was late in emerging, few statutory rules existed to guide the courts in distributing policy proceeds or other measure of value upon dissolution of the community.[15]

Thus, the basic problem faced by the courts of community property states in regard to life insurance policies is the formulation of a method for determining whether a policy is community or separate property and how, if deemed community property, it is to be divided

11. S. SCOVILLE, *supra* note 1, at 6.

12. *See id.* at 4-6; W. VANCE, *supra* note 8, at §§ 106, 108.

13. *See* Lang v. Commissioner, 304 U.S. 264, 266-67 (1938); Womack v. Womack, 141 Tex. 299, 301-02, 172 S.W.2d 307, 308 (1943); Thompson v. Calvert, 301 S.W.2d 496, 498 (Tex. Civ. App. 1957). *See also* S. SCOVILLE, *supra* note 1, at 5-6; Ray, *supra* note 6, at 835-36.

14. Life insurance policies were not amenable to community property treatment because they were peculiarly capable of being maintained by both separate and community funds with no indicia as to how community and separate interests were to be distinguished upon termination of the community or liquidation of the policy. *See* S. SCOVILLE, *supra* note 1; Nabors, *Civil Law Influences Upon the Law of Insurance in Louisiana—Life Insurance Problems Under the Community Property System*, 6 TUL. L. REV. 515, 515-17 (1932); Thurman, *Federal Estate and Gift Taxation of Community Property Life Insurance*, 35 TAXES 597, 597 (1957). *See generally* M. RUIZ, *supra* note 2.

15. Comment, *The Community Life Insurance Policy*, 18 BAYLOR L. REV. 627, 627 (1966). *See generally* Huie, *Community Property Laws as Applied to Life Insurance*, 17 TEX. L. REV. 121 (1939). For provisions governing the distribution of community property upon dissolution of the community, see TEX. CONST. art. 16.315 (1955); ARIZ. REV. STAT. ANN. § 14-3101 (1975); *id.* § 25-318 (Supp. Pamphlet 1973); CAL. CIV. CODE § 4800 (West Supp. 1976); CAL. PROB. CODE §§ 201-203 (West 1956), *as amended*, (West Supp. 1976); IDAHO CODE §§ 15-2-102, 32-712 (Supp. 1975); LA. CIV. CODE ANN. art. 136 (West 1952); NEV. REV. STAT. §§ 123.250, 125.150 (1975); *id.* § 134.010 (1973); N.M. STAT. ANN. §§ 29-1-9, 22-7-2, 22-7-6 (Supp. 1975); TEX. PROB. CODE §§ 45, 47(b), (e) (Vernon's Supp. 1975-76); WASH. REV. CODE ANN. § 11.04.015 (Supp. 1975); *id.* § 26.08.110 (1961).

upon dissolution of the marriage.[16] Life insurance may be acquired partly with separate and partly with community funds, since payment of the premiums usually spans a long period of time. Such a policy might be considered either separate or community property.[17] If the latter, it must be determined whether the community is entitled upon dissolution to the premiums, the proceeds, or the cash surrender value of the policy. Another difficulty which arises when community property consists wholly or partially of life insurance is determining its value for allocation purposes.[18] In the case of the marital community's dissolution upon divorce, value of the community interest could be measured by the value of the premiums paid on the policy from community funds,[19] the cash surrender value of the policy,[20] or some other formula.[21] In the case of the insured's death, the community might be entitled instead to share in the proceeds of the policy.

Confusion concerning the proper classification and valuation of life insurance policies for purposes of distribution has resulted in the development of three distinct legal approaches in the eight community property states.[22] Under the "premium tracing" doctrine the community upon dissolution is entitled to any enhancement in the value of the policy which is attributable to the payment of premiums with community funds.[23] The community is thus entitled to that percentage

16. When the community is dissolved by divorce, each spouse is allowed to keep his or her separate property and an equitable share of the community property. Armer v. Armer, 105 Ariz. 284, 463 P.2d 818 (1970); Kamrath v. Kamrath, 17 Ariz. App. 394, 498 P.2d 468 (1972); ARIZ. REV. STAT. ANN. § 25-318 (Supp. Pamphlet 1973). When the dissolution is caused by the death of a spouse, the decedent's one-half interest goes into his probate estate. *In re* Monaghan's Estate, 71 Ariz. 334, 227 P.2d 227 (1951); Blackman v. Blackman, 45 Ariz. 374, 43 P.2d 1011 (1935); La Tourette v. La Tourette, 15 Ariz. 200, 137 P. 426 (1914); ARIZ. REV. STAT. ANN. § 14-3101 (1975).

17. When community property includes a life insurance policy, the policy is often referred to as a community life insurance policy. The community is often considered to have an interest in the policy because of its contribution to the premiums. *See generally* Comment, *supra* note 15, at 627-38.

18. *See* Polk v. Polk, 228 Cal. App. 2d 763, 39 Cal. Rptr. 824 (Dist. Ct. App. 1964); McCurdy v. McCurdy, 372 S.W.2d 381 (Tex. Civ. App. 1963); Occidental Life Ins. Co. v. Powers, 192 Wash. 475, 479, 74 P.2d 27, 29 (1937). *See generally* W. DE FUNIAK & M. VAUGHN, *supra* note 1, at § 79; Huie, *Separate Ownership of Specific Property versus Restitution from Community Property in Louisiana*, 26 TUL. L. REV. 427 (1952); Comment, *supra* note 17, at 627-38.

19. *See* Succession of Lewis, 192 La. 734, 740, 189 So. 118, 120 (1939); McCurdy v. McCurdy, 372 S.W.2d 381, 384 (Tex. Civ. App. 1963).

20. *See* Comment, *supra* note 8, at 503-05.

21. *See id.*

22. The ensuing discussion will focus on California, Louisiana, New Mexico, Texas, and Washington. There is little or no case law on this subject in Idaho and Nevada, *see* S. SCOVILLE, *supra* note 1, at 171-80, and Arizona has used all the major approaches as well as created one of its own. *See id.* at 161-70.

23. *See* Polk v. Polk, 228 Cal. App. 2d 763, 781, 39 Cal. Rptr. 824, 835 (Dist. Ct. App. 1964); Wilson v. Wilson, 35 Wash. 2d 364, 366-67, 212 P.2d 1022, 1024-25 (1949); Small v. Bartyzel, 27 Wash. 2d 176, 178-80, 177 P.2d 391, 392-93 (1947); C. SMITH, *supra* note 3, § 21, at 34; Scoville, *Community Property Rights in Life Insurance*, 108 TRUSTS & ES. 1164, 1164-65 (1969).

of the policy's value which the premium payments from community funds bear to the total amount paid.[24] The courts of California and Washington generally use this method for determining the community's interest in a life insurance policy.[25] The federal courts also apply premium tracing in nearly all community property cases, regardless of the particular state court's position.[26] A second approach—followed in Louisiana,[27] Texas,[28] and New Mexico[29]—is the "inception of title" doctrine. Under this theory the character of a life insurance policy is determined by the nature of the funds used to pay the first premium.[30]

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24. For example, if a husband were to take out a $10,000 policy on his life, paying all the premiums with community funds, upon his death the community would be entitled to the entire $10,000 because the property was acquired entirely with community funds. *See* Polk v. Polk, 228 Cal. App. 2d 763, 781, 39 Cal. Rptr. 824, 835 (Dist. Ct. App. 1964); Small v. Bartyzel, 27 Wash. 2d 176, 178-80, 177 P.2d 391, 392-93 (1947). Thus, the surviving spouse would take his or her one-half community share, $5,000, and the insured's estate would take the other one-half. The insured having expressed his intent through the third-party beneficiary designation that the third party receive the proceeds, the third-party beneficiary would receive the insured's one-half community share. If, however, the husband were to pay 50 percent of the premiums with separate funds and 50 percent with community funds, the community would be entitled to only $5,000—the value of the property attributable to the use of community funds. *See* Metropolitan Life Ins. Co. v. Skov, 51 F. Supp. 470, 475-76 (D. Ore. 1943); McBride v. McBride, 11 Cal. App. 2d 521, 524-25, 54 P.2d 480, 481-82 (Dist. Ct. App. 1936). If dissolution occurred through divorce rather than death, the result would be similar, the community's share being based on the cash surrender value rather than the face value of the policy. *See* Forbes v. Forbes, 118 Cal. App. 2d 324, 325-26, 257 P.2d 721, 722-23 (Dist. Ct. App. 1953).

25. *See, e.g.*, Polk v. Polk, 228 Cal. App. 2d 763, 781, 39 Cal. Rptr. 824, 835 (Dist. Ct. App. 1964); Forbes v. Forbes, 118 Cal. App. 2d 324, 325-26, 257 P.2d 721, 722-23 (Dist. Ct. App. 1953); McBride v. McBride, 11 Cal. App. 2d 521, 524, 54 P.2d 480, 481-82 (Dist. Ct. App. 1936); Wilson v. Wilson, 35 Wash. 2d 364, 366-67, 212 P.2d 1022, 1024-25 (1949); Small v. Bartyzel, 27 Wash. 2d 176, 178-80, 177 P.2d 391, 392-93 (1947); *In re* Coffey's Estate, 195 Wash. 379, 384-85, 81 P.2d 283, 285-86 (1938).

26. Scoville, *supra* note 23, at 1165. *Compare* McCurdy v. McCurdy, 372 S.W.2d 381 (Tex. Civ. App. 1963), *and* Rowlett v. Mitchell, 52 Tex. Civ. App. 589, 114 S.W. 845 (1908), *with* Stapf v. United States, 189 F. Supp. 830, 833 (N.D. Tex. 1960), *and* Estate of Moody v. Commissioner, 42 B.T.A. 987 (1940). *But see* Parsons v. United States, 460 F.2d 228, 232-34 (5th Cir. 1972) (applying Texas law). Indeed, the federal courts' insistence on premium tracing apparently caused the state of Washington to change its position from inception of title to premium tracing. *Compare In re* Brown's Estate, 124 Wash. 273, 214 P. 10 (1923), *with* Shields v. Barton, 60 F.2d 351 (7th Cir. 1932), *and* Small v. Bartyzel, 27 Wash. 2d 176, 177 P.2d 391 (1947). *See also* Lang v. Commissioner, 304 U.S. 264 (1938).

27. The inception of title doctrine was first enunciated in *In re* Moseman, 38 La. Ann. 219 (1886), where the court held that a life insurance policy on which the first premiums were paid with separate funds was the husband's separate property despite his subsequent marriage. The community was found entitled only to reimbursement for premiums paid with community funds. *Id.* at 222. For a discussion of the community reimbursement concept, frequently interrelated with the doctrine of inception of title, see text & notes 32-34 *infra*. For subsequent Louisiana cases illustrating the inception of title doctrine, see Thigpen v. Thigpen, 231 La. 206, 231, 91 So. 2d 12, 21 (1956); Succession of Lewis, 192 La. 734, 189 So. 118 (1939); Succession of Verneuille, 120 La. 605, 45 So. 520 (1908).

28. Parson v. United States, 460 F.2d 228, 232-34 (5th Cir. 1972) (applying Texas law); McCurdy v. McCurdy, 372 S.W.2d 381 (Tex. Civ. App. 1963). The inception of title theory is used in Texas where the proceeds are claimed upon the insured's death; where dissolution is by divorce, however, Texas courts have used the premium tracing approach. *See* Berdoll v. Berdoll, 145 S.W.2d 227 (Tex. Civ. App. 1940).

29. *See In re* White's Estate, 41 N.M. 631, 73 P.2d 316 (1937); *accord*, Harris v. Harris, 83 N.M. 441, 493 P.2d 407 (1972); *In re* Miller's Estate, 44 N.M. 214, 100 P.2d 908 (1940).

30. C. SMITH, *supra* note 3, § 21, at 34-35. The time of inception generally is

Thus, the separate property character of a life insurance policy purchased initially with separate funds would not be affected by subsequent premium payments from community funds, even though payment of virtually all the premiums came from this source.[31] Finally, an approach usually used in conjunction with the inception theory to mitigate potential harsh results is the "community reimbursement" doctrine.[32] Under this approach, the community is entitled to reimbursement for all premiums paid with community funds.[33] The reimbursement approach is concerned only with the actual dollar amount of premiums paid with community funds, not the proceeds or cash surrender value of the policy.[34]

This Note will examine judicial treatment of life insurance policies upon dissolution of the community and suggest equitable approaches for allocating the proceeds or other value. Initially, theories governing allocation when dissolution is caused by death of the insured will be discussed, with separate treatment being given to policies naming the uninsured spouse as beneficiary and those designating some other party. The somewhat different problems arising when the community is dissolved by divorce will next be explored, followed by a discussion of judicial treatment of life insurance policies in this situation. Arizona's approach in each circumstance will be examined and recommendations made for possible changes in direction.

DISSOLUTION OF THE COMMUNITY BY REASON OF DEATH OF THE SPOUSE

Life insurance policies are a somewhat unique entity in that they contain elements of both contract and property. The promise of the

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deemed to be the time when the first premium is paid. *See* Berry v. Franklin State Bank & Trust Co., 186 La. 623, 173 So. 126 (1937); Succession of Verneuille, 120 La. 605, 45 So. 520 (1908); Note, *Community Property—Life Insurance—Application of the Inception of Title Doctrine*, 18 Sw. L.J. 521, 522 (1964).

31. Berry v. Franklin State Bank & Trust Co., 186 La. 623, 173 So. 126 (1937); Succession of Verneuille, 120 La. 605, 45 So. 520 (1908); *In re* Moseman, 38 La. Ann. 219 (1886); Rowlett v. Mitchell, 52 Tex. Civ. 589, 114 S.W. 845 (1908); Ray, *supra* note 6, at 894.

32. *See* Succession of Lewis, 192 La. 734, 740, 189 So. 118, 120 (1939); McCurdy v. McCurdy, 372 S.W.2d 381, 384 (Tex. Civ. App. 1963); C. SMITH, *supra* note 3, § 21, at 34-35. The inception of title approach is not always accompanied by the reimbursement doctrine. *See* Rowlett v. Mitchell, 52 Tex. Civ. 589, 114 S.W. 845 (1908).

33. *See* Succession of Lewis, 192 La. 734, 740, 189 So. 118, 120 (1939); Succession of Verneuille, 120 La. 605, 609, 45 So. 520, 522 (1908); Nabors, *supra* note 14, at 540. *But see* Hogan v. Hall, 118 F.2d 247, 249 (5th Cir. 1941) (since widow had received one-half of the community estate, reimbursement was not necessary); Sizeler v. Sizeler, 170 La. 128, 131, 127 So. 388, 389 (1930) (terms of insurance policy, not community property law, governed). *See generally* W. DE FUNIAK & M. VAUGHN, *supra* note 1, § 79, at 190-91 (presenting the premium tracing doctrine as superior to the reimbursement approach); Huie, *supra* note 18.

34. *See* Succession of Lewis, 192 La. 734, 740, 189 So. 118, 120 (1939); Succession of Verneuille, 120 La. 605, 609, 45 So. 520, 522 (1908); McCurdy v. McCurdy, 372 S.W.2d 381, 384 (Tex. Civ. App. 1963).

insured to pay premiums to the insurer in exchange for the insurer's promise to pay proceeds to a beneficiary upon the insured's death is purely contractual. On the other hand, the policy is also property. It is an investment of funds. It may be used as collateral for a loan, surrendered for cash, sold, or given away.[35] When a court is faced with the problem of deciding whether or not the terms of the agreement have been met and whether or not the insurer or insured owe any further obligations to one another, the contractual elements of the policy are paramount. This contract analysis is necessary, for instance, when the insurer refuses to pay the proceeds upon death of the insured due to an alleged breach of the contract by the insured.[36] On the other hand, when the court is asked to determine who is entitled to what proportion of the proceeds or cash surrender value of the policy, in addition to ascertaining who, according to the terms of the contract, is entitled to receive, the court must determine whether the contractual terms of disbursement are in harmony with the applicable property law.[37] In this latter situation, where the policy terms conflict with the relevant property law, the property law generally is controlling.

The time at which community property interests in life insurance policies become relevant is upon dissolution of the community.[38] In situations where the community has been dissolved by death, the issue which causes the most difficulty is determining what interest, if any, the community has in the proceeds of a life insurance policy which has been paid for totally or partially with community funds. The degree of such interest will determine the amount of proceeds the community can claim. Where some or all of the proceeds are found to be community property, the surviving spouse takes one-half of such proceeds and the named beneficiary takes the other community half through the interest therein of the insured's estate.[39] The beneficiary also receives those proceeds to which the community is found not entitled.[40]

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35. J. GRIEDER & W. BEADLES, *supra* note 7, at 362.

36. *See, e.g.*, Prudential Ins. Co. v. Barnes, 285 F.2d 299 (9th Cir. 1960); Marks v. Mutual Life Ins. Co., 96 F.2d 267 (9th Cir. 1938); New York Life Ins. Co. v. Greber, 55 Ariz. 261, 100 P.2d 987 (1940), *aff'd on rehearing*, 61 Ariz. 341, 149 P.2d 671 (1944).

37. *See, e.g.*, Mesa Oil Co. v. Business Men's Assurance Co., 476 F.2d 491 (9th Cir.), *cert. denied*, 414 U.S. 1003 (1973); Greber v. New York Life Ins. Co., 61 Ariz. 341, 149 P.2d 671 (1944); Droz v. Paul Revere Life Ins. Co., 1 Ariz. App. 581, 405 P.2d 833 (1965).

38. *See* ARIZ. REV. STAT. ANN. §§ 14-6114, -6201 (1975); id. § 25-318 (Supp. Pamphlet 1973).

39. *See* Mundt v. Connecticut Gen. Life Ins. Co., 35 Cal. App. 2d 416, 95 P.2d 966 (Dist. Ct. App. 1939); New York Life Ins. Co. v. Bank of Italy, 60 Cal. App. 602, 214 P. 61 (Dist. Ct. App. 1923).

40. *See* Gettman v. City of Los Angeles, 87 Cal. App. 2d 862, 197 P.2d 817 (Dist. Ct. App. 1948); Modern Woodmen v. Gray, 113 Cal. App. 729, 299 P. 754 (Dist. Ct. App. 1931).

Determining the community interest in life insurance where the community is dissolved by divorce presents more complex problems. In divorce situations the court is concerned with determining the relative property rights of the divorcing spouses in an ongoing policy. The concern is not how the proceeds should be disbursed, as they are not yet due; rather it is what interests the divorcing spouses have in the policy itself or its cash surrender value, if any. Determinations made at this stage may result in restrictions being placed on the ultimate distribution of proceeds;[41] surrender of the policy for cash, each spouse taking his or her community share of the cash and the insurance contract being terminated;[42] or the insured's paying the uninsured spouse his or her community share out of some other separate property, thus extinguishing the uninsured spouse's interest in the policy.[43]

An important factor in determining the distribution of policy proceeds upon the insured's death is the intent of the deceased. A beneficiary designation in an insurance policy is treated much the same as a provision in a will, the effectuation of the decedent's intent being considered paramount.[44] Barring fraud or an unjust result, the insured should be permitted to exercise his right to designate a beneficiary,[45] regardless of the character of the funds used to pay premiums on the policy. While the community may be entitled to some sort of property interest in an insurance policy paid for with community funds, it does not necessarily follow that this interest must be realized through a share of the proceeds. There are other alternatives available for ensuring that the community will receive an equitable portion of the estate. So long as the insured has through some means guaranteed his or her spouse an equitable share of the community property,[46] the intent to benefit a particular person through the insurance policy ought to be enforced.[47]

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41. *See* text accompanying note 119 *infra.*
42. *See* text & note 125 *infra.*
43. *See* text & notes 123-24 *infra.*
44. Shields v. Barton, 60 F.2d 351, 354 (7th Cir. 1932); Gaethje v. Gaethje, 8 Ariz. App. 47, 51, 442 P.2d 870, 874, 7 Ariz. App. 544, 549, 441 P.2d 579, 584 (1968) [this case having been reported twice hereinafter will be cited only to the report in 8 *Arizona Appeals Reports*]; Continental Ins. Co. v. Madonia, 205 La. 828, 830, 18 So. 2d 310, 312 (1944).
45. *See* Franklin Life Ins. Co. v. Mast, 290 F. Supp. 671, 674 (D. Ariz. 1968), *rev'd on other grounds,* 435 F.2d 1038 (9th Cir. 1970); Doss v. Kalas, 94 Ariz. 247, 252, 383 P.2d 169, 172 (1963); *cf.* ARIZ. REV. STAT. ANN. § 20-1128 (1975).
46. The testator may designate other property to be devised to his or her spouse in order to guarantee that the spouse receives a just portion and the court may do this for the testator if he fails to give the surviving spouse a fair share. Gaethje v. Gaethje, 8 Ariz. App. 47, 51, 442 P.2d 870, 874 (1968). The same result could be achieved by the insured through the use of joint tenancy; he need only put a fair share of the property into a joint tenancy with his spouse.
47. Both husband and wife have the right to leave by testamentary disposition one half of the community property however he or she may choose. . . . Joint

These basic principles assume, however, that the use of community funds to purchase the policy has not been accomplished through fraud. The uninsured spouse has no cause to object to distribution of insurance proceeds to the beneficiary where payments from community funds were made with his or her consent. In most cases such consent is present, and in fact it is presumed by statute in Arizona where one of certain specified relatives is the beneficiary.[48] Where the use of community funds or the changing of the beneficiary[49] is without such consent, a finding of fraud may be possible. Lack of consent, however, is not the only form of fraud.

Fraud also may be found where the uninsured's consent has been secured by deception; for instance, by a misrepresentation of who will be the beneficiary.[50] In such cases it cannot be said that it was both spouses' intent that the named beneficiary receive the proceeds under the policy. Deliberate deception of this nature is referred to as active fraud, and has been held in most states to destroy the beneficiary designation as to half the proceeds.[51] In Washington active fraud voids the the beneficiary designation entirely.[52] These drastic results obtain because the uninsured's consent to the use of community funds was based upon misrepresentations by the insured. In such a situation the consenting spouse's intent in consenting to the payments from community funds—that he or she be the recipient of the proceeds—ought to be

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tenancy is a commonly used device for passing title to survivors as are trust instruments. Life insurance is a method of converting present assets into property to be distributed in accordance with the insured's directions at death. We fail to see why any one of these methods is inherently more fraudulent than any other or why any such transfers should be ignored in determining whether the deceased spouse "defrauded" the surviving spouse by the designation of a beneficiary on a life insurance policy.

Id. at 51, 442 P.2d at 874.

48. ARIZ. REV. STAT. ANN. § 20-1128(C) (1975) (child, grandchild, parent, brother, or sister of either spouse).

49. *See* Warthan v. Haynes, 155 Tex. 413, 419, 288 S.W.2d 481, 484 (1956). The changing of the named beneficiary on the policy without the uninsured spouse's consent is the only type of fraud which has been addressed by the courts.

50. Fraud might also be found where the uninsured spouse is deceived as to the existence of the policy or its value.

51. *See, e.g.*, Mundt v. Connecticut Gen. Life Ins. Co., 35 Cal. App. 2d 416, 421, 95 P.2d 966, 969 (Dist. Ct. App. 1939); New York Life Ins. Co. v. Bank of Italy, 60 Cal. App. 602, 604-07, 214 P. 61, 62-63 (Dist. Ct. App. 1923); Sizeler v. Sizeler, 170 La. 128, 131-33, 127 So. 388, 389-90 (1930).

52. *See* Occidental Life Ins. Co. v. Powers, 192 Wash. 475, 484-86, 74 P.2d 27, 31-32 (1937). This result is easily altered in Washington by naming the insured's estate as beneficiary, then devising the decedent's one-half community property interest to the third party by will. This circumvention of the law of fraud, though blatant, has been found permissible under the husband's exercise of his power of management. *In re* Towey's Estate, 22 Wash. 2d 212, 155 P.2d 273 (1945). Thus, in Washington if the husband desires to make his mother beneficiary of the policy and cannot get his wife's consent, he need only name his estate beneficiary and devise the proceeds to his mother. Until 1972 the wife could not use this method as she had no power to manage community property in Washington. S. SCOVILLE, *supra* note 1, at 127, 133. The wife now has equal management rights. WASH. REV. CODE ANN. § 26.16.030 (Supp. 1975).

enforced.[53] The insured's estate or third-party beneficiary should not be allowed to benefit by the insured's fraudulent act.

If no fraud is proven, however, the court should assume the surviving spouse knew of and consented to the designation of the insured's estate as beneficiary. To require more would both complicate the management of community and separate funds and often abort the valid community intent to assign insurance proceeds to a third party. The most frequently recurring situation where these questions must be addressed is where the insured's death has brought to bear the insurer's contractual obligation to pay the proceeds on the policy.

Spouse as Beneficiary

Where the uninsured spouse is named beneficiary of an insurance policy paid for with community funds, few problems arise. Because death of either spouse terminates the existence of the community,[54] it results in each spouse's half of the community property becoming separate property.[55] Thus the question is merely whether the uninsured spouse can retain the entire proceeds of the insurance policy without the need for probate. Those community property states with case law addressing this situation have held that policies naming the surviving spouse as beneficiary are the separate property of the surviving spouse regardless of whether the premiums were paid with separate or community funds; the community has no right to reimbursement for premiums paid.[56] The insured spouse is deemed to have made a gift of his or her one-half interest in the policy to the surviving spouse, and through principles of merger, the entire proceeds become the separate property of the survivor-beneficiary.[57]

Although Arizona has no case law dealing with this situation, it is addressed statutorily with the result being the same as that reached judicially in other states.[58] It is difficult to envision an approach which

53. *See* Wilson v. Wilson, 35 Wash. 2d 364, 367-68, 212 P.2d 1022, 1024-25 (1949); Occidental Life Ins. Co. v. Powers, 192 Wash. 475, 483-85, 74 P.2d 27, 31-32 (1937).

54. *See, e.g.*, ARIZ. REV. STAT. ANN. § 14-3101 (1975); LA. CIV. CODE ANN. art. 136 (West 1952); N.M. STAT. ANN. § 29-1-9 (Supp. 1975); WASH. REV. CODE ANN. § 11.04.015 (Supp. 1976).

55. Tway v. Payne, 55 Ariz. 343, 345-47, 101 P.2d 455, 456-57 (1940); Hanrahan v. Sims, 20 Ariz. App. 313, 317, 512 P.2d 617, 621 (1973); *In re* Pfeffer's Estate, 16 Ariz. App. 147, 150, 492 P.2d 27, 30 (1971); ARIZ. REV. STAT. ANN. § 14-3101(A) (1975). Such disbursement is the responsibility of the administrator who will divide the property in line with the deceased's testamentary intent and relevant statutory restrictions. *Id.* § 14-3703.

56. Estate of Miller, 23 Cal. App. 2d 16, 71 P.2d 1117 (Dist. Ct. App. 1937); Hall v. Toussaint, 52 La. Ann. 1763, 28 So. 304 (1900); *In re* Miller's Estate, 44 N.M. 214, 217, 100 P.2d 908, 910 (1940); Warthan v. Haynes, 155 Tex. 413, 420, 288 S.W.2d 481, 484 (1956). *See also* Huie, *supra* note 15, at 127; Comment, *supra* note 8, at 499-500.

57. Brown v. Lee, 371 S.W.2d 694, 696 (Tex. 1963). *See generally* S. SCOVILLE, *supra* note 1, at 26-28, 67-68, 93-96, 126, 156-57.

58. The Arizona statute provides that where the surviving spouse is the named bene-

would be more equitable or would better carry out the intent of the parties. Further, the insurer, absent conflicting property law, is contractually obligated to pay all the proceeds to the named beneficiary, in this case the surviving spouse. Since the interest in protecting the community is served if the surviving spouse receives all the proceeds, there is no need for community property law to alter the contractual obligation in this situation.

Someone Other Than Spouse as Beneficiary

A frequent area of dispute over life insurance proceeds is where the insured has named his estate or some third person as beneficiary under a life insurance policy. In such situations, at the insured's death the uninsured spouse may claim ownership of part or all of the proceeds of the policy on the grounds that they are his or her separate or community share of the property. These problems become especially acute where the beneficiary is changed without the uninsured spouse's knowledge, or where the uninsured spouse has been eliminated as a beneficiary in a surprise move by the insured spouse. The courts are not unified in their treatment of proceeds in this situation.

Inception of Title. As noted previously, Louisiana, Texas, and New Mexico employ the inception of title theory to determine the interests in life insurance where premiums have been paid with mixed funds.[59] The only knowledge necessary to determine ownership through application of this doctrine is the character of the funds with which the initial premium was paid, as the policy unalterably takes on the character of such funds.[60] Essentially, the use of this doctrine is based on considerations of uniformity and simplicity.[61] Also influential

ficiary on a policy insuring the life of the deceased spouse, the beneficiary spouse takes the proceeds as his or her separate property. *See* ARIZ. REV. STAT. ANN. § 20-1128(A) (1975). Life insurance proceeds under this statute do not pass through probate; the decedent's one-half interest is viewed as a gift to the beneficiary and not a testamentary devise, thus becoming the beneficiary survivor's separate property. *See id.; cf.* Coe v. Winchester, 43 Ariz. 500, 33 P.2d 286 (1934). If, in the absence of such a provision, the proceeds were instead considered a devise, creditors could indirectly get at this money if there were no other community property in the estate or if the community were exhausted by costs of administration, funeral expenses, taxes, or homestead allowance. *See* ARIZ. REV. STAT. ANN. §§ 14-3805, -3902 (1975). Where a beneficiary spouse's interest in property depends upon his or her surviving the other spouse and both spouses die simultaneously, absent evidence that the beneficiary spouse survived the other spouse, the beneficiary spouse will be deemed to have predeceased the insured. *Id.* §§ 14-2808, 20-1127.

59. *See* Thigpen v. Thigpen, 231 La. 206, 91 So. 2d 12 (1956); *In re* White's Estate, 41 N.M. 631, 73 P.2d 316 (1937); McCurdy v. McCurdy, 372 S.W.2d 381 (Tex. Civ. App. 1963).

60. *See* cases cited notes 27-30 *supra*.

61. Note, *supra* note 30, at 525. Whether uniformity and simplicity are in themselves sufficient virtues to warrant wholesale adoption of the doctrine is at least open to debate. There may also be lingering in this doctrine a view of the policy as a contract entered into by the initial payor, whose death leaves only payment of the proceeds

is the rationale that in community property jurisdictions any item of property must be designated either community or separate property at dissolution of the community.[62] Most property, being capable of purchase by a single payment which generally consists of either community or separate funds, is amenable to designation according to the character of the funds used to purchase the property. This is a simple approach and easy to apply. Because of its simplicity and the fact that it is capable of uniform application, Louisiana, Texas, and New Mexico have generally applied it across the board to all types of property.[63] Unfortunately, since life insurance is generally not purchased with one lump sum but rather with numerous premiums paid over long periods of time, classification according to purchase funds does not fit neatly into this system. Judicial reliance on inception of title in such cases, therefore, may not always be the most equitable approach.[64] The life insurance policy in some respects is a long term investment, capable of being maintained by commingled separate and community funds. Thus, the characterization of the policy and its proceeds as separate or community according to the character of the funds used to pay the first premium is not always indicative of the true nature of the investment. Under the inception of title approach, if a policy designating someone other than the spouse as beneficiary is first purchased with separate funds, it becomes the insured's separate property,[65] and the surviving spouse has no interest in the proceeds of the policy upon the insured's death.[66]

Seemingly incongruous is the Louisiana and Texas courts' departure from their general acceptance of the inception of title doctrine where the premiums are paid entirely with community funds and a third

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to the beneficiary in order for performance on both sides to be complete. The difficulty with the inception of title theory is that it can lead to the separate estate of the insured receiving a gift or an interest-free loan from the community depending on whether or not the reimbursement approach also is used. Also, if an overwhelming percentage of the total premiums paid were paid with community funds, the application of the inception of title doctrine could operate as a constructive fraud on the rights of the other spouse. *Id.* at 525-26; *cf.* Martin v. Moran, 11 Tex. Civ. App. 509, 510, 32 S.W. 904, 905 (1895).

62. *See* ARIZ. REV. STAT. ANN. § 14-3101(A) (1975).

63. Scoville, *supra* note 23, at 1164.

64. *See* Succession of Lewis, 192 La. 734, 189 So. 118 (1939) (application of the inception of title doctrine required policy proceeds be paid to insured's estate even though community funds had paid for $909.36 worth of premiums); Martin v. Moran, 11 Tex. Civ. App. 509, 32 S.W. 904 (1895) (inception of title doctrine defeated an otherwise valid devise despite a lack of evidence that the spouse had objected to the devise or had not received her fair share of community property); Note, *supra* note 30, at 525-26.

65. See text & notes 27-33 *supra.*

66. But see text & notes 32-34 *supra.* There are no cases where the first premium was paid with community funds and the rest with separate funds. However, if such a case should arise, under a strict application of the inception of title doctrine, the proceeds ought to be classified community property. Such an application, as in the converse factual situation, may very well create gross inequities.

party is the beneficiary. In this situation these courts refuse to find any community property interest in a third-party beneficiary insurance policy.[67] This departure seems to result from the fact that in all the cases disputing rights in insurance proceeds in these states the insured was the husband.[68] Thus, the third-party beneficiary designation was found to be a valid exercise by the husband of his power of management and control over community property.[69] These courts hold that the designation of a third party as beneficiary by the insured spouse is a valid gift by the community; the surviving spouse, therefore, has no interest in the life insurance policy or its proceeds.[70] The only limitation on this power to make a community gift is that the insured spouse may not make such a gift in fraud upon the survivor's rights.[71] Unfortunately, this rule offers little protection to the unsuspecting spouse because courts seldom find fraud to exist[72] and have failed to set down objective criteria for determining when fraud would exist.[73] The Louisiana and Texas courts also have held that the community is not even allowed reimbursement for the community funds used to pay the premiums where no fraud was present.[74]

Premium Tracing. While Louisiana, Texas, and New Mexico show reluctance to classify a single item of property as both community

67. *See, e.g.*, Pearce v. National Life & Accident Ins. Co., 12 La. App. 608, 609-10, 125 So. 776, 777-78 (1930); Brown v. Lee, 371 S.W.2d 694, 696 (Tex. 1963); Alexander v. Alexander, 410 S.W.2d 275, 277 (Tex. Civ. App. 1966); Comment, *supra* note 15, at 497-99; Note, *supra* note 2, at 630. *See generally* S. SCOVILLE, *supra* note 1, at 70-71, 96-100. Were the insured's estate the named beneficiary, however, the proceeds would be considered community property. Thigpen v. Thigpen, 231 La. 206, 91 So. 2d 12 (1956); S. SCOVILLE, *supra* at 71, 100. The proceeds are also considered community property where the husband's secret concubine is named beneficiary. *See* Touissant v. National Life & Accident Ins. Co., 147 La. 977, 86 So. 415 (1920).

68. *See, e.g.*, Thigpen v. Thigpen, 231 La. 206, 234, 91 So. 2d 12, 15 (1956); Succession of Lewis, 192 La. 734, 738, 189 So. 118, 119 (1939); McCurdy v. McCurdy, 372 S.W.2d 381, 382 (Tex. Civ. App. 1963).

69. *See* Brown v. Brown, 282 S.W.2d 90, 92 (Tex. Civ. App. 1955).

70. *See* Pearce v. National Life & Accident Ins. Co., 12 La. App. 608, 609-11, 125 So. 776, 777-78 (1930); Brown v. Lee, 371 S.W.2d 694, 696 (Tex. 1963); Alexander v. Alexander, 410 S.W.2d 275, 277 (Tex. Civ. App. 1966).

71. Davis v. Prudential Ins. Co., 331 F.2d 346, 352 (5th Cir. 1964) (interpreting Texas law); Krueger v. Williams, 163 Tex. 545, 548, 359 S.W.2d 48, 50 (1962); Watson v. Harris, 61 Tex. Civ. App. 263, 272, 130 S.W. 237, 241 (1910). The determination of whether or not the uninsured spouse has been defrauded is made on a case-by-case basis. S. SCOVILLE, *supra* note 1, at 97. When fraud is found, the result also is determined using a case-by-case method; depending on the circumstances, the uninsured may receive all the proceeds, Moore v. California-Western States Life Ins. Co., 67 S.W.2d 932 (Tex. Civ. App. 1934) (the widow received all the proceeds, only $3,000, probably because she was left very little by her husband otherwise), or half the proceeds. Aaron v. Aaron, 173 S.W.2d 310 (Tex. Civ. App. 1943).

72. *See, e.g.*, Sizeler v. Sizeler, 170 La. 128, 129-30, 127 So. 388, 389-90 (1930); Sherwood v. New York Life Ins. Co., 166 La. 829, 831, 118 So. 35, 37 (1928); Brown v. Brown, 282 S.W.2d 90, 92 (Tex. Civ. App. 1955); Jones v. Jones, 146 S.W. 265, 268 (Tex. Civ. App. 1912). *See also* Comment, *supra* note 15, at 630-32; Comment, *supra* note 8, at 497-99.

73. S. SCOVILLE, *supra* note 1, at 97.

74. *See* Hogan v. Hall, 118 F.2d 247, 249 (5th Cir. 1941) (interpreting Louisiana law); Rowlett v. Mitchell, 52 Tex. Civ. 589, 114 S.W. 845 (1908); S. SCOVILLE, *supra* note 1, at 70, 96; W. VANCE, *supra* note 8, at § 105.

and separate, no similar aversion is found in the courts of California and Washington. These states use premium tracing to determine policy ownership when the community has been dissolved by death.[75] Under this approach the proceeds are treated as part separate property and part community property according to the percentage of premiums paid with each type of funds.[76] This approach focuses upon the investment character of a life insurance policy. It looks at each premium paid into the policy as an investment towards the ultimate payment of the proceeds. As a result, the community and separate estates are deemed entitled to that portion of the proceeds that funds from each created in the form of premiums.[77] Exceptions are recognized only where the surviving spouse expressly consents, in writing, to the designation,[78] or the designation is in exchange for consideration from the beneficiary.[79] Unless one of these two exceptions is present, the third-party beneficiary designation is considered invalid in California to the extent of the surviving spouse's one-half community property interest.[80] In Washington the third-party beneficiary designation is generally deemed totally invalid on the grounds that the surviving spouse's interest in community property is vested, and not a mere expectancy.[81] The surviving spouse thus receives all of the proceeds paid for with the community funds.[82]

Reimbursement. Rather than a proportionate share of the proceeds, the community receives the exact dollar amount of the premiums paid from community funds under the reimbursement theory,[83] generally used in conjunction with the inception of title doctrine. The surviving spouse would take one-half of that reimbursed as his or her community share and the named beneficiary would take

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75. *See* Polk v. Polk, 228 Cal. App. 2d 763, 781, 39 Cal. Rptr. 824, 835 (Dist. Ct. App. 1964); Small v. Bartyzel, 27 Wash. 2d 176, 178-80, 177 P.2d 391, 392-93 (1947).

76. See text & note 24 *supra*. The portion attributable to the decedent's separate funds probably would be deemed to belong to the designated beneficiary as an inter vivos, nontestamentary gift. *See* Wilson v. Wilson, 35 Wash. 2d 364, 212 P.2d 1022 (1949); Small v. Bartyzel, 27 Wash. 2d 176, 177 P.2d 391 (1947).

77. *See* cases cited note 25 *supra*.

78. *See* New York Life Ins. Co. v. Bank of Italy, 60 Cal. App. 602, 214 P. 61 (Dist. Ct. App. 1923); Occidental Life Ins. Co. v. Powers, 192 Wash. 475, 483-85, 74 P.2d 27, 31 (1937); S. SCOVILLE, *supra* note 1, at 28.

79. *See* Dixon Lumber Co. v. Peacock, 217 Cal. 415, 417-18, 19 P.2d 233, 234 (1933); Johnston v. Johnston, 182 Wash. 573, 47 P.2d 1048 (1935).

80. Tyre v. Aetna Life Ins. Co., 54 Cal. 2d 399, 404, 353 P.2d 725, 728, 6 Cal. Rptr. 13, 16 (1960), *noted in* 49 CALIF. L. REV. 544 (1961); Britton v. Hammell, 4 Cal. 2d 690, 691-93, 52 P.2d 221, 222-23 (1935); Blethen v. Pacific Mut. Life Ins. Co., 198 Cal. 91, 99-101, 243 P. 431, 434-35 (1926). This is analogous to the result reached in Texas and Louisiana where the courts disallow the third-party designation due to fraud. See text & note 71 *supra*.

81. S. SCOVILLE, *supra* note 1, at 128.

82. *See* King v. Prudential Ins. Co., 13 Wash. 2d 414, 125 P.2d 282 (1942); Occidental Life Ins. Co. v. Powers, 192 Wash. 475, 484-86, 74 P.2d 27, 31-32 (1937).

83. *See* cases cited note 33 *supra*.

the other half,[84] it presumably being the insured's intent that whatever interest he had in the policy go to the beneficiary. This approach both protects the insured's intent in distributing the proceeds to the insured's named beneficiary, and protects the uninsured spouse to the extent of at least returning his or her community share of the premiums paid into the policy.

Arizona's Fourth Approach. The Arizona courts have followed no single approach consistently.[85] In the 1972 case of *Perry v. Perry*[86] the Arizona court of appeals followed an inception of title approach in denying the community a share of life insurance proceeds. The insured had purchased two life insurance policies before marrying, naming his mother as beneficiary on both policies.[87] The premiums on the policies were paid entirely with separate funds.[88] When the insured's widow later claimed an interest in the policies, the court applied the inception of title doctrine to find that both policies were purchased prior to marriage and were therefore the insured's separate property.[89] Although it seems clear that the court was applying inception of title,[90] it was in fact unnecessary for it to do so as none of the premiums were paid with community funds; thus the community had no substantial basis for asserting an interest in the proceeds.

The *Perry* decision represented a sharp diversion from the prior decision of the Arizona supreme court in *Gristy v. Hudgens*,[91] where the court appeared to reject the three traditional approaches in favor of a fourth, distinct theory. The insured spouse in *Gristy* had changed the beneficiary of his life insurance policy, which apparently had been paid for at least partially with community funds, without his wife's knowledge or consent.[92] The Arizona court held that in the absence of a showing of fraud on the wife's community rights,[93] or that she had

84. See text & notes 32-34 *supra.*

85. Typical of this confusion is Horton v. Horton, 35 Ariz. 378, 278 P. 370 (1929), where the Arizona supreme court simultaneously applied both the inception of title and premium tracing rules in determining whether certain real estate was separate or community property.

86. 18 Ariz. App. 299, 501 P.2d 568 (1972).

87. *Id.* at 300, 501 P.2d at 569.

88. *Id.* All the premiums on one policy were paid by the mother from her own funds, and the premiums on the other policy were paid entirely from a Marine Corps pension plan granted to the insured for services rendered before his marriage. *Id.*

89. *Id.* The court also stated that, since none of the premiums were paid with community funds, the community had no lien on the proceeds for reimbursement of premiums. *Id.*

90. Even if the court had applied premium tracing, the same result would have followed because 100 percent of the premiums were paid with separate funds. Due to the opinion's reference to reimbursement, however, *id.*, and its emphasis of the fact that the policy was purchased prior to marriage, *id.*, it appears that the court was applying the inception of title doctrine.

91. 23 Ariz. 339, 203 P. 569 (1922).

92. *Id.* at 341, 203 P. at 570.

93. The Arizona supreme court surprisingly reached its result by ignoring a well-

received less than her fair share of community property,[94] the named beneficiary was entitled to all the proceeds.[95]

In a more recent case, *Gaethje v. Gaethje*,[96] the Arizona court of appeals apparently followed *Gristy*,[97] rejecting the approaches used in other community property states[98] in favor of a polished restatement of the *Gristy* holding.[99] The court held that where the insured changes the beneficiary designation without the uninsured spouse's consent, there will be no presumption of fraud if it can be shown that upon the insured's death the surviving spouse received an amount of property equal to at least one-half of all community property.[100] Although the uninsured spouse in *Gaethje* received none of the proceeds of a term life insurance policy paid for entirely with community funds,[101] she did receive property equivalent to the amount of the insurance proceeds through other means.[102] Under such circumstances, according to the court, the third-party beneficiary designation will be enforced.[103] The court noted, however, that if the surviving spouse does not receive an equitable share of the community property, the insured, in effect, has

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established rule that property is presumed paid with community funds absent contrary evidence. *See* King v. Uhlmann, 103 Ariz. 136, 151, 437 P.2d 928, 943 (1968); Benson v. Hunter, 23 Ariz. 132, 202 P. 233 (1921); *In re* Klumpke's Estate, 167 Cal. 415, 424, 139 P. 1062, 1065 (1914); Oylear v. Oylear, 35 Idaho 732, 208 P. 857 (1922); Strong v. Eakin, 11 N.M. 107, 66 P. 539 (1901); *In re* Curtis' Estate, 116 Wash. 237, 244, 199 P. 309, 312 (1921); G. McKAY, THE LAW OF COMMUNITY PROPERTY § 206 (2d ed. 1925).

94. The court relied on the lack of any showing that premiums were paid with community funds after the first 4 years of the insured's 10-year marriage, the beneficiary designation not having been changed until 5 years after the premiums ceased to be paid from community funds. 23 Ariz. at 341, 348, 203 P. at 570, 572.

95. *Id.* at 348, 203 P. at 572. This holding was based upon Arizona statutory law which, until 1973, gave the husband sole power of dominion and control over personal community property. *See* Ariz. Rev. Stat. Ann. § 25-211 (1956) (repealed 1973). The husband, therefore, could dispose of personalty belonging to the community as he saw fit, so long as he did not defraud his wife. Under the new statute, both spouses have equal powers to control and manage all the community property, personalty, and realty. *See* ARIZ. REV. STAT. ANN. § 25-214 (Supp. Pamphlet 1973). Presumably, the rule as to fraud now applies to both spouses in their management of the property.

96. 8 Ariz. App. 47, 442 P.2d 870 (1968). The husband had named a son from a previous marriage as beneficiary of a term life insurance policy, after having first named his second wife. *Id.* at 48, 442 P.2d at 871.

97. The *Gaethje* court expressly relied on *Gristy*. *Id.* at 49-50, 442 P.2d at 872-73.

98. The inception of title doctrine, see text & notes 27-31 *supra*, reimbursement, see text & notes 32-34 *supra*, and premium tracing approaches, see text & notes 23-26 *supra*, were analyzed. 8 Ariz. App. at 49, 442 P.2d at 872.

99. *See* 8 Ariz. App. at 49-52, 442 P.2d at 872-75.

100. *Id.* at 52, 442 P.2d at 875. The court held the life insurance proceeds to be part of the total community property from which the uninsured spouse was required to receive an equitable share. *Id.*

101. *See id.*

102. *See id.* Other means of distributing a fair share to the surviving spouse would include testamentary devises by the insured to the surviving spouse. The insured also could place property in a trust with the surviving spouse as beneficiary. Creation of joint tenancy in property, sharing the tenancy with the surviving spouse, is another possibility. Finally, the surviving spouse might receive a fair share of the community property through intestate succession.

103. *Id.*

worked a constructive fraud and the deficiency must be made up from the policy proceeds.[104] A second interesting aspect of *Gaethje* was the court's use of a "last premium" rule to determine the nature of the policy.[105] The court held that the last payment is the one responsible for keeping the policy in force at the insured's death and thus the character of the funds used to pay that premium determines the character of the proceeds.[106] Here the most recent premiums had been paid with community funds; hence the proceeds were a part of the community.

In *Lock v. Lock*,[107] the Arizona court of appeals again disregarded the inception of title and premium tracing doctrines and relied on the second part of the *Gaethje* rule to determine the character of a policy. Here the insured failed to carry out a divorce settlement obligation to maintain a term life insurance policy for the benefit of the children of the marriage.[108] The *Lock* court, looking to *Gaethje,* found that although premiums had initially been paid with community funds, separate funds had paid for all the coverage in existence at the insured's death.[109] The community funds were viewed as having "paid a premium for a risk long since expired"[110] and the last premium paid, which represented the realized risk of death, as determining the character of the proceeds.[111]

Thus, today in Arizona, under the *Gaethje-Lock* rule, a third-party beneficiary designation will stand, even absent the uninsured spouse's consent, so long as upon the insured's death the uninsured spouse receives through joint tenancy, devise, intestate succession, or otherwise at least one-half the value of the total community property.[112] To

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104. *Id.*

105. This approach has been advocated by Professor Huie. Huie, *Community Property and Life Insurance—Substantive Aspects—Developments in Texas,* 2 TEX. INSTITUTES 118, 128 (1957). See text & notes 106-11 *infra.*

106. The *Gaethje* court stated that a term policy has no monetary value until the death of the insured. Thus, "[t]he fact that the husband's separate estate paid a premium for a risk long since expired without loss should not give his separate estate any vested interest in these proceeds." 8 Ariz. App. at 52, 442 P.2d at 875.

107. 8 Ariz. App. 138, 444 P.2d 163 (1968).

108. *Id.* at 139-40, 444 P.2d at 164-65.

109. *Id.* at 145, 444 P.2d at 169.

110. *Id.*

111. *Id.; accord,* Sherman v. Roe, 153 Tex. 1, 7, 262 S.W.2d 393, 397 (1953). *See also* S. SCOVILLE, *supra* note 1, at 167. The first part of the *Gaethje* rule was not applicable here as the insured had long since divorced the plaintiff, thus owing no obligation to provide for her at his death.

112. The Arizona supreme court apparently has not yet addressed this question.

The most recent application of the *Gaethje* rule occurred in Guerrero v. Guerrero, 18 Ariz. App. 400, 402-03, 502 P.2d 1077, 1079-80 (1972). The husband changed the beneficiary of a term life insurance policy from his wife to his niece without his wife's knowledge or consent. *Id.* at 401, 502 P.2d at 1078. Premiums were paid with community funds, the wife's separate funds, contributions from the husband's employer, and the husband's social security benefits. *Id.* As a result, the court found the policy to be community property. Moreover, it was found that the husband had worked a constructive fraud on his wife, entitling her to all the proceeds of the life insurance policy. She whatever extent the uninsured spouse does not receive one-half of the total community property the insured has worked a constructive fraud and the uninsured spouse is entitled to whatever proportion of the life insurance proceeds necessary to bring his or her share up to one-half. Further, the characterization of life insurance proceeds as separate or community property is determined not by the nature of the funds used to pay the first premium but by the nature of the funds used to pay the last premium. This is at least true where the policy is a term life insurance policy with no cash surrender value. If the policy has a cash surrender value, then it may be said that throughout its existence it has a property value in which parties may have an interest. The probable result in Arizona where the insured dies leaving life insurance proceeds payable to a third-party beneficiary on a policy which has a cash surrender value would be the court's application of the first part of the *Gaethje* rule, disregarding the latter as inapplicable. A term life policy, on the other hand, is of no value to anyone until the insured dies and then has value only if all the premiums were paid up until the death. Thus the term life policy until the insured's death is more of a contract than it is property, and it is the payment of the last premium which is responsible for keeping the policy in force at the insured's death and thereby entitling the beneficiary to payment of the proceeds.

Recommendations. Due to the confusing and inconsistent case law in the area of third-party beneficiaries, it is difficult to determine which of the approaches produces the most equitable result. The Louisiana and Texas inception of title approach appears inadequate to protect the surviving spouse from being defrauded by such a designation. This is particularly true where the policies, without consent, are purchased with community funds since in most such situations the court finds the designation not fraudulent, but rather a permissible gift of community property.[113] The premium tracing approach also seems inequitable in that it always gives to the surviving spouse an interest in the life insurance policy proceeds proportionate to the premiums paid with community funds, even if he or she consented to the designation and received an ample share of other community property.[114]

was also held entitled to all the community property plus the decedent's separate property since her one-half community interest was less than \$3,500—the statutory minimum then allowed a surviving spouse. *See id.* at 403, 502 P.2d at 1080. This result was mandated by statute and is still applicable, though the \$3,500 amount has been increased to \$15,500. *See* ARIZ. REV. STAT. ANN. §§ 14-2401 to -2403, -3973 (1975).

113. *See* text & notes 60-67 *supra.*

114. *See* Polk v. Polk, 228 Cal. App. 2d 763, 781, 39 Cal. Rptr. 824, 835 (Dist. Ct. App. 1964) (even though there was no fraud in the insured's designation of his brother as beneficiary, and his wife had abandoned him 12 years earlier, the wife under premium tracing was found to have an interest in the proceeds); Small v. Bartyzel, 27 Wash. 2d 176, 179-80, 177 P.2d 391, 392-93 (1947) (where community funds used for

Thus, it is possible under this rule for the legitimate intent of the deceased to be defeated by a surviving spouse who has in no way been wronged.[115]

The *Gaethje* approach presents the most equitable of the alternatives, and with a few adjustments should be followed in Arizona. The first and most dramatic adjustment suggested is that the "last payment" aspect of the rule be abandoned. If a substantial portion of the premiums on a life insurance policy have been paid with community funds over the objection of the uninsured spouse, the uninsured spouse should be found to have an interest in the policy proceeds if he or she has not already received an equitable portion of the community property. This legitimate interest should not be defeated simply because the last premium was paid with the insured's separate funds. This second part of the *Gaethje* rule has all the inadequacies of the inception of title doctrine.

A further adjustment in the rule would be to require a careful and detailed explanation by the courts as to their method for determining whether or not the uninsured has received an equitable share of the community property. Such an explanation would aid insureds in their estate planning by establishing definite standards for them to follow in providing for their spouses so as to ensure that third-party beneficiary designations will be upheld. It will also allow uninsured spouses contemplating court action to determine with greater certainty whether they have any rights in the proceeds. Finally, the courts ought to explain fully the circumstances which will give rise to a finding of fraud. Currently, proving fraud is especially difficult in Arizona since there is a statutory presumption that the surviving spouse has consented to a third-party beneficiary designation where the named beneficiary is related to the insured.[116] The presumption will fail only if there is an affirmative showing sufficient to negate the presumption or if constructive fraud as defined in *Gaethje* is shown.[117]

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premiums on policy having insured's daughter by prior marriage as designated beneficiary, wife allowed one-half of proceeds of policy taken out by insured before marriage even though wife did not object to such use of community funds).

115. This violates the traditional rule that the decedent's wishes will be honored whenever possible. *See* ARIZ. REV. STAT. ANN. § 14-2603 (1975). Beneficiary designations in insurance policies are generally treated as will provisions, the intent of the decedent being considered paramount. Shields v. Barton, 60 F.2d 351, 354 (7th Cir. 1932); Gaethje v. Gaethje, 8 Ariz. App. 47, 51, 442 P.2d 870, 874 (1968); Continental Ins. Co. v. Madonia, 205 La. 828, 834-35, 18 So. 2d 310, 312 (1944).

116. ARIZ. REV. STAT. ANN. § 20-1128(C) (1975); *see* Gaethje v. Gaethje, 8 Ariz. App. 47, 52-53, 442 P.2d 870, 875-76 (1968). For further discussion of section 20-1128, see text & note 48 *supra*. In *Gaethje* the lower court had granted the wife summary judgment. The Arizona court of appeals found the evidence inadequate to rebut the statutory presumption that the surviving spouse had consented to the third party designation, and the granting of summary judgment to the wife was therefore held erroneous. 8 Ariz. App. at 53, 442 P.2d at 876.

117. 8 Ariz. App. at 52, 442 P.2d at 875. In the case of a third-party beneficiary

Where the third-party beneficiary designation is a fraud because the surviving spouse was led to believe he or she was the named beneficiary, the defrauded spouse should be awarded the entire proceeds.[118] Because of the potential detrimental reliance and the extreme culpability of the deceased's actions, the surviving spouse's expectancy in the proceeds should be fulfilled.

DISSOLUTION OF THE COMMUNITY BY REASON OF DIVORCE

In determining ownership of community versus separate life insurance policies it is important to distinguish between dissolution of the community by death and dissolution by divorce. When the community is dissolved by divorce, the problem that arises concerns ownership or allocation of the cash surrender value of the policy,[119] or the policy itself, rather than the policy proceeds. Unlike the situation where the insured has died, the life insurance contract is in full force and the insurer's contractual obligation to pay proceeds under the policy has not yet matured. Thus, the relative property interests are in the current value of the policy itself and not in the proceeds.

At dissolution of the community by divorce there is no reason for prolonging each spouse's realization of his or her interest; if the policy is to remain in force, the divorce may cause the insured to desire a change in the beneficiary. Moreover, a policy with a cash surrender value is capable of liquidation at divorce; it has a current, easily ascertainable value; and finally, it is susceptible to ready ascertainment of the relative community and separate property interests in it. A policy without a cash surrender value, while not capable of liquidation at divorce and thus lacking a specific current value, is nonetheless susceptible to ready ascertainment of the relative community and separate property interests in it, measured by total premiums paid on the policy.

policy where premiums are paid with community funds, so long as the spouse knows and consents to the designation, it is equitable that the intent of the parties be carried out. Absent express consent, such as a writing, or failure to challenge a third-party beneficiary designation by the surviving spouse the court has only the word of the uninsured to support a finding that there was no consent to a third-party beneficiary designation. It is better in such situations that a statutory presumption of consent be enforced and the third-party beneficiary designation permitted. It is not unreasonable to assume that the uninsured spouse would have knowledge of any expenditure of community funds and that failure to object to a third-party designation indicates assent. This is especially true where the spouse subsequently ratified the act by not challenging the disbursement to the named beneficiary.

118. See text accompanying notes 50-53 *supra.*

119. *See generally* S. SCOVILLE, *supra* note 1, at 22, 41-44, 55, 87-89, 109, 118, 124-25. This type of settlement is, of course, most easily applied to policies having some present value at the time of divorce, such as a cash surrender value. See discussion note 7 *supra.* This need not always be the case, however, as long as some value can be put on the policy at divorce—such as the total dollar value of premiums paid on the policy to date.

Such a policy also has both contract and property characteristics: the insurer is contractually obligated to pay the proceeds upon death of the insured, and it is possible for the uninsured spouse to have a property interest in both the proceeds and the policy where community funds have been used to pay premiums. Further, all life insurance policies are investments of sorts and because of this ought to be considered property when the community is dissolved by divorce. If the premiums on the policy were paid with community funds, it is—at least to some extent—a community investment, the community's interest in which ought to be recognized.

Inception of Title. When the first premiums are paid with separate funds,[120] Louisiana courts closely adhere to the inception of title doctrine, designating the policy the separate property of the insured.[121] These courts, however, will generally allow the community to be reimbursed for any premiums paid with community funds at least where the insured's estate is the named beneficiary.[122] Where the policy has been paid for exclusively with community funds, however, the law is sparse and unclear; three different approaches have been suggested. Under one theory, based on the reimbursement doctrine, either spouse takes the policy as separate property and reimburses the other for one-half of the premiums paid with community funds.[123] The spouse taking the policy can then name the beneficiary of his or her choice.[124] A second possibility is for the spouses to split the cash surrender value of the policy after its cancellation at divorce.[125] Finally, the insured may keep the policy as his or her separate property while giving the uninsured spouse one-half of the actual value of the policy upon the community's dissolution.[126] The determination of actual value is to be made by using such factors as the cash surrender value

120. This classification includes policies purchased before marriage which remain separate property, as well as policies purchased after marriage with separate funds. *See* W. DE FUNIAK & M. VAUGHN, *supra* note 1, at § 79.

121. Though the cases on divorce are sparse to nonexistent, the operation of the inception of title doctrine is the same in both death and divorce situations. For examples of this doctrine and how it works, see Berry v. Franklin State Bank & Trust Co., 186 La. 623, 637, 173 So. 126, 131 (1937); Succession of Verneuille, 120 La. 605, 45 So. 520 (1908); Succession of Buddig, 108 La. 406, 408, 32 So. 361, 362 (1902); *In re* Moseman's Estate, 38 La. Ann. 219 (1886).

122. For examples of the reimbursement doctrine and how it is used, see Succession of Lewis, 192 La. 734, 740, 189 So. 118, 120 (1939); Succession of Verneuille, 120 La. 605, 609, 45 So. 520, 522 (1908); *cf.* McCurdy v. McCurdy, 372 S.W.2d 381, 384 (Tex. Civ. App. 1963). Another approach which has been used is to split the cash surrender value of the policy between the spouses. *See* Comment, *supra* note 8, at 503-04.

123. *See* Daigre v. Daigre, 228 La. 682, 83 So. 2d 900, *rev'd on other grounds*, 230 La. 472, 89 So. 2d 41 (1956); Comment, *supra* note 8, at 503-04.

124. *See* Comment, *supra* note 8, at 503-04.

125. *See* Daigre v. Daigre, 230 La. 472, 89 So. 2d 41 (1956); Comment, *supra* note 8, at 504.

126. *See* Comment, *supra* note 8, at 503-05.

of the policy and the life expectancy of the insured.[127] The difference in treatment where the community is dissolved by divorce rather than death undoubtedly is caused by the community's greater property interest in the policy prior to death of the insured.[128]

Premium Tracing. Case law concerning the application of the premium tracing rule to life insurance policies in divorce situations is either nonexistent or confused. Some premium tracing jurisdictions have not had the opportunity to apply the doctrine to this particular problem.[129] Assuming the premium tracing rule was used, the community would appear to be entitled to the proportion of the policy's cash surrender value created by community funds.[130] The doctrine has been applied in this manner by California where the uninsured spouse was the named beneficiary.[131] Due to the fact that the court need only divide community property between spouses equitably upon divorce,[132] however, it is not uncommon for doctrines such as premium tracing to be disregarded in that situation in favor of a more flexible approach. Thus, other premium tracing jurisdictions have departed from their usual form of analysis. Where all premiums are paid with community funds and there is no disposition of the policy in the divorce settlement, Washington and New Mexico courts have taken the position that the spouses hold the policy as tenants in common.[133] Such an approach results in both spouses owning an undivided interest as joint beneficiaries under the policy, with the power to designate anyone they wish as beneficiary of their share of the proceeds. If no beneficiary is named, the interest passes to their respective heirs at death. This may result in a significant inequity, as where the community pays only a small proportion of the premiums before divorce, the remainder being paid by the insured after divorce; application of the above rule in such a case would give to the uninsured spouse an equal interest in the life insurance policy with the insured, despite the disparity in contribution.

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127. *See* Huie, *supra* note 15, at 143; Comment, *supra* note 8, at 504. Actual value is not cash surrender value, but rather the value which might, hypothetically, be placed on the policy if it were sold to a third person. An analysis is made of the amount of premiums paid as compared to the life expectancy of the insured, the value being determined at "such a sum as, at a reasonable rate of compound interest, would equal the face of the policy at the end of the period of expectancy." Huie, *supra* at 143 n.88, *quoting* Supreme Lodge Knights of Pythias v. Neeley, 135 S.W. 1046, 1050 (Tex. Civ. App. 1911).

128. See text at pp. 201-02 *supra*.

129. *See* S. SCOVILLE, *supra* note 1, at 26. Property settlements often are worked out by the divorcing spouses, and thus there is little litigation regarding the specific treatment of life insurance policies.

130. See text accompanying notes 23-27 *supra*.

131. *Cf. In re* Jafeman, 29 Cal. App. 3d 244, 257-58, 105 Cal. Rptr. 483, 491 (Dist. Ct. App. 1972). *See also* Blaine v. Blaine, 63 Ariz. 100, 109, 159 P.2d 786, 790 (1945).

132. *See* ARIZ. REV. STAT. ANN. § 25-318 (Supp. Pamphlet 1973).

133. *In re* Miller's Estate, 44 N.M. 214, 216, 100 P.2d 908, 910 (1940) (dictum); Northwestern Life Ins. Co. v. Perrigo, 47 Wash. 2d 291, 294-95, 287 P.2d 334, 336 (1955); S. SCOVILLE, *supra* note 1, at 118, 155.

The Arizona Position. Arizona lacks consistency in its treatment of insurance policies in divorce situations. In its first case on the subject, *Rothman v. Rumbeck,*[134] the Arizona supreme court applied the inception of title and reimbursement rules. In this case the insured purchased a life insurance policy with separate funds, later naming his first wife as beneficiary and paying premiums with community funds.[135] After divorce, he changed the policy to make his estate the beneficiary.[136] The court, while holding that a policy initially purchased with separate funds remains the separate property of the insured, allowed the first wife to be reimbursed for one-half of the premiums paid with community funds.[137] Thus the court in *Rothman,* as in *Perry v. Perry,*[138] used the inception of title theory to determine the character of the policy, but required that the wife be reimbursed.[139] The court reversed its position in *Blaine v. Blaine.*[140] Here, as in *Rothman,* the insured purchased and paid premiums on a life insurance policy prior to marriage,[141] later paying premiums with community funds.[142] In a subsequent divorce action, the Arizona court utilized premium tracing rather than the inception of title rule,[143] finding the community entitled to credit for the increase in cash surrender value of the life insurance policy occasioned by the use of community funds to pay the premiums.[144]

Arizona thus has used both the inception of title and premuim tracing approaches. Inception of title was used in a case brought at the insured's death, while the premium tracing approach was applied in regard to the divorce and property settlement itself. There has been no express overruling of either of these cases. Since *Gaethje v. Gaethje,*[145] according to the facts of the case, rejected premium tracing and inception of title only as to third-party beneficiaries in death situations,[146] either approach might be applied in the future. The Arizona statute governing division of property at divorce,[147] which seems to

134. 54 Ariz. 443, 96 P.2d 755 (1939).
135. *Id.* at 444-45, 96 P.2d at 755-56.
136. *Id.* at 445, 96 P.2d at 756.
137. *Id.* at 452, 96 P.2d at 759. The court also noted that if the policy was community property and not divided upon dissolution of the first marriage, the spouses would hold the policy as tenants in common. *Id.* at 454, 96 P.2d at 759. See text accompanying note 133 *supra.*
138. 18 Ariz. App. 299, 501 P.2d 568 (1972). See text & notes 86-90 *supra.*
139. The court thus followed the position of the Louisiana and Texas courts. See text & notes 32-33 *supra.*
140. 63 Ariz. 100, 159 P.2d 786 (1945).
141. *Id.* at 103, 159 P.2d at 788.
142. *Id.* at 104-05, 159 P.2d at 788.
143. *Id.* at 109-10, 159 P.2d at 790.
144. *Id. See also* S. SCOVILLE, *supra* note 1, at 162.
145. 8 Ariz. App. 47, 52, 442 P.2d 870, 875 (1968).
146. *Id.* at 48, 442 P.2d at 871.
147. ARIZ. REV. STAT. ANN. § 25-318 (Supp. Pamphlet 1973).

follow the spirit of the *Gaethje* rule,[148] would seem to require that a life insurance policy, if deemed community property, be considered part of the total community property to be equitably divided between the spouses at divorce.

Recommendations. Where the uninsured spouse is the named beneficiary, the premium tracing rule, utilized in *Blaine v. Blaine,*[149] seems to distribute most equitably the community insurance policy in divorce situations and should be followed consistently in Arizona. It allows the insured to retain the policy, as well as name the beneficiary, while permitting the uninsured to recover his or her community share of the cash surrender value of the policy. Since the uninsured spouse is the named beneficiary on the policy, he or she should receive more than just reimbursement for community funds used to pay premiums on the policy. It was the intent of both spouses that the uninsured spouse receive the proceeds on the policy, and the uninsured's consent to paying premiums with community funds may well have been based on the expectation that he or she would receive the proceeds of such an investment.

The insured also has interests in the policy that can best be protected by such a method. Where the community is dissolved by divorce, it is unlikely that the insured would want to continue the policy with the ex-spouse as the named beneficiary. Thus the insured ought to have the election of either continuing or discontinuing the policy, but in either case the uninsured should receive at least one-half of the current value of the policy. If the policy has no cash surrender value, however, and the uninsured spouse is the named beneficiary, reimbursement is the remedy most closely equivalent to premium tracing. Under this remedy the insured spouse would retain the right to name a new beneficiary while the uninsured recovered his or her share of the amount of community funds spent on the policy. Application of the reimbursement theory thus would ensure compensation of the community for the amount of premiums paid with community funds.[150]

Absent fraud, where the named beneficiary on a policy paid for with community funds is the insured's estate or a third party rather than

148. Section 25-318 requires the court, upon dissolution of marriage to divide the spouses' community property "equitably, though not necessarily in kind. . . ." *Id.* This, like the *Gaethje* rule, requires no set formula or approach be used by the court. So long as each spouse has received a fair share of the community property, the property distribution will not be questioned.

149. 63 Ariz. 100, 159 P.2d 786 (1945).

150. The premium tracing and reimbursement doctrines do not produce widely divergent results, as it is generally recognized that the cash surrender value of a life insurance policy is roughly equivalent to the total amount of premiums paid plus interest. *See* Early v. Atkinson, 175 F.2d 118, 122 (4th Cir. 1949); Prudential Ins. Co. v. Howell, 29 N.J. 116, 122-23, 148 A.2d 145, 148 (1959).

the spouse, Arizona courts should apply an approach paralleling *Gaethje* and section 25-318 of the Arizona statutes.[151] That is, each spouse should receive an equitable portion of the total community property. In order to determine to what extent the community has an interest in a life insurance policy for this purpose, the court should apply the reimbursement theory. This is not to say that the policy must be sold or cashed in, but only that in figuring the total value of community property to be divided, the court should consider the total amount of premiums paid on the policy with community funds to be a part of the total community property value. Although reimbursement is usually applied in conjunction with the inception theory, here it is recommended that a reimbursement theory of valuation be applied without regard to the nature of the funds used to pay the first premium. So long as at least one premium was paid with community funds the reimbursement approach should be applied.

CONCLUSION

The case law on community property rights in life insurance policies, particularly in Arizona, is both confusing and inconsistent. In dealing with this conflicting area of law, states have applied three different rules, each with its own advantages and defects, depending upon the factual situation involved. Adopting one approach for all situations for purposes of simplicity, however, can produce harsh and inequitable results. A flexible approach such as that aimed at in *Gaethje* and in section 25-318 of the Arizona statutes allows the courts to ensure an equitable result while preserving to the maximum extent the insured's beneficiary designation. Further refinements of this approach will provide Arizona with an appropriate framework for treating community interests in life insurance.

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151. ARIZ. REV. STAT. ANN. § 25-318 (Supp. Pamphlet 1973).